

**FISCAL NOTE**  
**SB 1 - HB 2**  
**SECOND EXTRAORDINARY SESSION**

November 3, 1999

**SUMMARY OF BILL:** Provides various changes to Tennessee's tax structure as follows:

1. Reduces the general sales tax from 6% to 3.75% except for sales tax on hotels, motels, amusements, rental cars, tobacco and alcohol products. (Effective 3-1-00)
2. Repeals the state sales tax on grocery food. (Effective 3-1-00)
3. Provides for a tax of 3.75% on adjusted gross income with exemption levels for various taxpayers. (Effective 1-1-00) Employers may begin withholding and remitting the tax after January 1, 2000 but no later than the first payroll period which ends after March 31, 2000 with amounts being withheld to spread the withholding equally over all remaining payroll periods of the calendar year.
4. Repeals the Hall Income Tax. (Effective 1-1-00)
5. Makes various changes in the Inheritance and Gift Taxes. (Effective 1-1-00)
6. Increases the Excise Tax from 6% to 6.5%. (Effective 1-1-00)
7. Provides for a credit against the Professional Privilege Tax. (Effective 1-1-00)
8. Repeals the Excise Tax on certain *pass-through* entities.
9. Allows credit for franchise tax for LLC and LLP filing fees.
10. Provides for the single item limitation on local sales tax to apply only to motor vehicles, boats and airplanes. (Effective 3-1-00)

**ESTIMATED FISCAL IMPACT:**

**Increase State Revenues - Net Impact - \$566,300,000 First Full Year**  
**\$623,170,000 FY99-00**

**Increase State Expenditures – Dept. of Revenue:**  
**\$11,725,600 FY99-00 (7 mos.)**  
**\$28,098,400 FY 00-01**

**Increase Local Govt. Revenues – Exceeds \$20,000,000**

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	<u>1<sup>st</sup> Full Year</u>	<u>FY99-00</u>
<u>State Revenues Increased</u>		
Flat tax (net of exemptions & deductions)	\$2,544,000,000	\$1,221,120,000
Excise tax	<u>55,500,000</u>	<u>27,750,000</u>
Subtotal – Revenues Increased	\$2,599,500,000	\$1,248,870,000

**Less:**

State Revenues Reduced

Repeal state sales tax on food	258,000,000	86,000,000
Reduction in general sales tax rate	1,529,200,000	509,700,000
Repeal Hall Income Tax	169,000,000	-
Reform Gift & Inheritance Taxes	2,000,000	-
Eliminate Double Taxation on Businesses	60,000,000	30,000,000
Credit Against Professional Tax	<u>15,000,000</u>	
Subtotal – Revenues Reduced	<u>2,033,200,000</u>	<u>625,700,000</u>
Net Increase in State Revenues	<u>\$566,300,000</u>	<u>\$623,170,000</u>

Assumptions for Changes in State Revenues:

1. **Flat Tax** – The first full year reflects a rate of 3.75% on adjusted gross income, exemption levels as outlined in the bill, 1998 income data (adjusted), capital gains taxed at 50% and a 10% compliance factor. The amount estimated for FY99-00 assumes collections of 48% of the first full year since employers will be allowed to begin withholding at any time from 1/1/00 to the first payroll after 3/31/00.
2. **Excise Tax** – The increase assumes the value per ½ % of the current budgeted estimate of excise tax collections for the FY2000 budget.
3. **Sales Tax**
  - Repeal of sales tax on food – The estimate for the first full year represents the value of the grocery rate reduction remaining after the reduction in the general sales tax rate from 6% to 3.75%. The estimate for FY99-00 represents four months collection (April-July) since the effective date for this provision is 3-1-00.
  - Reduction in sales tax rate on all but selected items – The estimate for the first full year represents a 2.25% reduction in items outlined in the bill and considers those items already at special tax rates that would not be affected. The estimate for FY99-00 represents four months collection (April-July) since the effective date for this provision is 3-1-00.

4. **Hall Income Tax** – This figure represents estimated collections for FY00-01 and does not reflect any decreases for the current fiscal year due to the year in which such taxes are due.
5. **Gift & Inheritance Taxes** – The estimate assumes changes in the bill that would reduce collections for FY00-01 but will not affect current year collections.
6. **Double Taxation on Businesses** – The estimate reflects an amount that will not be collected due to revisions in this bill and assumes 50% will be realized in the current fiscal year.
7. **Credit against Professional Tax** – The first full year estimate represents the credit received by in-state professionals. It is estimated that the current year will not be affected, since the credit will be realized on tax returns filed on or after April 15, 2001.
8. The net increase in state revenues does not consider funds which would be provided to the Rainy Day Fund by passage of this bill since existing statutes require 10% of the estimated growth in revenues to be allocated to such fund.

Assumptions for State Expenditures:

1. The estimate for FY99-00 represents funding for seven months with \$8,964,000 for recurring items and \$2,761,600 for computers, workstations, printers, furniture, training, and other one-time type expenses. It is estimated that 291 additional positions will be added in various divisions throughout the Department of Revenue to carry out provisions of the bill.
2. The estimate for FY00-01 is an amount of approximately \$27,000,000 for recurring costs and \$1,098,400 for one-time expenses not incurred during FY99-00. An additional 139 full-time positions throughout the department are estimated to be needed and 190 part-time positions in the Processing Division to assist in tax returns filed after January 1, 2001.
3. The estimated recurring expenditures for FY00-01 represent an increase in recurring needs of \$18,036,000 over FY99-00, since the program will be fully functional at some point during the fiscal year beginning July 1, 2000.
4. The additional positions will be established as needed at various times during FY99-00 and FY00-01; therefore, recurring expenses will not be fully realized until FY01-02 and are estimated to be approximately \$30,000,000 utilizing 430 full-time positions and 190 part-time positions.

A summary of expenditures is shown below:

	<u>FY99-00</u>	<u>FY00-01</u>	<u>FY01-02 &amp; thereafter</u>
Recurring	\$8,964,000	\$27,000,000	\$30,000,000
One-Time	<u>2,761,600</u>	<u>1,098,400</u>	<u>                    </u>
Total	\$11,725,600	\$28,098,400	\$30,000,000

Local Government Revenues:

Provisions of the bill removing the single item limitation on local sales tax except for motor vehicles, boats and airplanes is estimated to provide additional revenues to local governments exceeding \$20,000,000.

**CERTIFICATION:**

This is to duly certify that the information contained herein is true and correct to the best of my knowledge.



James A. Davenport, Executive Director